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UNCLAS SECTION 01 OF 03 ANKARA 006199

SIPDIS

SENSITIVE

STATE FOR E, EB/IFD, EUR/SE
TREASURY FOR OASIA - DLOEVINGER, MMILLS, JLEICHTER
NSC FOR BRYZA AND MCKIBBEN

E.O. 12958: N/A

TAGS: [EFIN](#) [EAID](#) [EINV](#) [PREL](#) [PGOV](#) [TU](#)

SUBJECT: MEETING WITH TREASURY U/S CANAKCI

REF: A. ANKARA 6141

[1](#)B. ANKARA 6162

[1](#)C. ANKARA 6165

[1](#)1. (SBU) SUMMARY: IN A MEETING WITH ECONOFFS, TURKISH TREASURY U/S CANAKCI DESCRIBED THE STILL-EARLY STATE OF PLAY WITH THE IMF SIXTH REVIEW MISSION. CANAKCI CLAIMED THE GOT WAS ON TRACK TO MEET OR GET CLOSE TO END-YEAR INFLATION, GROWTH AND FISCAL TARGETS. HE WAS ALSO OPTIMISTIC ABOUT ACHIEVING A 6.5 PERCENT PRIMARY SURPLUS IN 2004. ON KEY STRUCTURAL REFORMS, ESPECIALLY THOSE INVOLVING LEGISLATION, PROGRESS WAS SLOWER. ON DIRECT TAX REFORM, CANAKCI WAS OPTIMISTIC THAT THEY ARE NEARING AGREEMENT WITH THE FUND ON A COMPROMISE. CANAKCI CLAIMED THE GOT HAD RECOMMITTED TO MOVING FORWARD ON WORLD BANK-PROPOSED STRUCTURAL REFORMS AFTER THE IMF REVIEW IS COMPLETE. HE CONFIRMED THAT THE U.S. FINANCIAL AGREEMENT HAD NOT YET BEEN PROPOSED TO THE COUNCIL OF MINISTERS AND PROVIDED NO INDICATION OF WHEN IT MIGHT BE PROPOSED, NOTING THE GOT HAD ADEQUATE CASH-FLOW FOR THE TIME BEING. END SUMMARY.

END-YEAR MACRO TARGETS WITHIN REACH:

[1](#)2. (SBU) ECONOFFS MET WITH TREASURY UNDERSECRETARY IBRAHIM CANAKCI OCTOBER 2 TO GET AN UPDATE ON PROGRESS ON ECONOMIC REFORMS. CANAKCI CHARACTERIZED DISCUSSIONS WITH THE IMF SIXTH REVIEW MISSION--CURRENTLY IN ANKARA--AS GOING WELL BUT STILL AT AN EARLY STAGE. DESPITE THE SECOND QUARTER SLOWDOWN IN GDP GROWTH, WHICH WAS PARTLY ATTRIBUTABLE TO THE WAR, CANAKCI EXPRESSED CONFIDENCE TURKEY WOULD ATTAIN ITS 5 PERCENT 2003 GDP GROWTH TARGET. CANAKCI CITED INDUSTRIAL PRODUCTION DATA SUGGESTING THAT THE PACE OF GROWTH HAD PICKED UP BEGINNING IN JUNE. ON INFLATION, CANAKCI WAS SIMILARLY CONFIDENT ABOUT MEETING THE YEAR-END TARGET, SAYING THAT THE WHOLESALE PRICE INDEX MIGHT ACTUALLY BEAT THE 20 PERCENT TARGET AND COME IN AROUND 18 PERCENT FOR THE YEAR. THE CURRENT ACCOUNT DEFICIT, ON THE OTHER HAND, MIGHT BE SLIGHTLY HIGHER THAN THE 3.2 PERCENT OF GDP PROJECTED AT THE TIME OF THE FIFTH REVIEW.

FISCAL SITUATION AND 2004:

[1](#)3. (SBU) CANAKCI SAID THEY ARE GOING THROUGH THE END-AUGUST FISCAL DATA WITH THE IMF TEAM, ALTHOUGH THEY STILL LACK FULL PUBLIC SECTOR-WIDE NUMBERS, INCLUDING FROM SEE'S. HE ASSERTED THAT THE GOT MIGHT REACH ITS END-AUGUST FISCAL TARGET OR ONLY HAVE A SLIGHT DEVIATION. IT WAS MORE MEANINGFUL, HOWEVER, TO FOCUS ON THE FULL YEAR, SINCE THE MONTH-T0-MONTH NUMBERS CAN BE MISLEADING DUE TO SEASONAL OR SPECIAL CIRCUMSTANCES. ONE SUCH EXAMPLE COULD BE FOUND IN THE NEGATIVE IMPACT ON THE JULY NUMBERS CAUSED BY FRONT-LOADING SOME EXPENDITURES THAT WOULD NORMALLY HAVE TAKEN PLACE IN AUGUST AND SEPTEMBER. THIS EXPLAINED THE SHARP IMPROVEMENT IN THE MONTHLY PRIMARY SURPLUS FROM JULY TO AUGUST. CANAKCI CLAIMED THE GOT'S STUDIES SHOW THAT TURKEY WILL ACHIEVE THE FULL-YEAR 6.5 PERCENT PRIMARY SURPLUS TARGET.

[1](#)4. (SBU) WITH GOT AND IMF OFFICIALS IN INTENSIVE CONSULTATIONS ON THE NUMBERS, CANAKCI EXPECTED THE BROAD OUTLINES OF THE 2004 BUDGET AND A CLEARER PICTURE OF THE END-YEAR FISCAL PROJECTION TO BE READY BY MONDAY. HIGH PLANNING COUNCIL MEETINGS ON OCTOBER 8 AND 11 WOULD FURTHER CLARIFY THE BUDGET TO BE PROPOSED TO PARLIAMENT BY OCTOBER [1](#)7. CANAKCI STATED THAT BOTH THE IMF AND GOT BELIEVE THAT, IF THERE IS ANY SHORTFALL IN REVENUE, THERE IS ROOM TO MAKE UP FOR THIS BY CUTTING EXPENDITURES. THOUGH THE

UNANTICIPATED STRENGTH OF THE LIRA HAD RESULTED IN LOWER VAT COLLECTIONS, THIS WAS OFFSET BY THE EXCHANGE RATE'S POSITIVE EFFECT ON CERTAIN EXPENDITURES. HE ALSO DISAGREED WITH ANALYSTS' CONTENTION THAT THE RELIANCE ON ONE-OFF MEASURES WILL CREATE SERIOUS PROBLEMS IN ATTAINING 2004 FISCAL TARGETS. HE EXPLAINED THAT THE ONE-OFF MEASURES AMOUNTED TO ABOUT 2.7 PERCENT OF GNP BUT THAT ALMOST HALF OF THEM, SUCH AS THE SPECIAL COMMUNICATIONS TAX AND THE SPECIAL TRANSACTIONS TAX, COULD EASILY BE REPEATED. MOREOVER, IN 2004 THE GOT EXPECTS TO SEE THE FULL-YEAR IMPACT OF 2003 BUDGET CUTS IN HEALTH AND SOCIAL SECURITY, AS WELL AS THE STAFF REDUCTIONS IN SEE'S. CANAKCI DENIED THAT LOWER GAS PRICES OR EARLY PAYMENTS OF CIVIL SERVICE BONUSES WOULD INTERFERE WITH THE GOT REACHING ITS FISCAL TARGET. THE GAS PRICE REDUCTION STEMMED FROM LOWER COSTS, AND THE TL 160 TRILLION (USD 114 MILLION) BONUS PAYMENTS--IF PAID EARLY--WOULD BE OFFSET.

PARASTATAL STAFF REDUCTION:

15. (SBU) CANAKCI ADMITTED THE GOT HAD ONLY REDUCED REDUNDANT POSITIONS AT STATE ECONOMIC ENTERPRISES BY 12,000 OUT OF THE 19,400 TARGETED IN THE IMF PROGRAM BY THE END OF SEPTEMBER, 2003. CANAKCI POINTED OUT THAT A PORTION OF THE SHORTFALL--AT LEAST 3,000 POSITIONS--STEMMED FROM THE DELAY IN THE TEKEL PRIVATIZATION WHICH WAS ORIGINALLY SCHEDULED FOR THE THIRD QUARTER OF 2003 AND NOW WOULD TAKE PLACE IN THE FOURTH QUARTER. CANAKCI ALSO CLAIMED THAT THE GOT HAD IN SOME CASES REDUCED STAFF IN EXCESS OF COMPANY-SPECIFIC TARGETS, BUT THAT THE IMF DID NOT GIVE THE GOT CREDIT FOR THESE ADDITIONAL REDUCTIONS. THE GOT IS NOW WORKING WITH THE IMF TO GET CREDIT FOR THESE REDUCTIONS BY COMMITTING NOT TO REHIRE. TO FURTHER REDUCE PUBLIC SECTOR STAFFING, THE GOT IS STUDYING THE POSSIBILITY OF PROVIDING ADDITIONAL INCENTIVE PAYMENTS FOR YEAR-2003 RETIREMENT BY ANY OF THE 33,000 PUBLIC SECTOR EMPLOYEES ELIGIBLE FOR RETIREMENT.

DIRECT TAX REFORM:

16. (SBU) CANAKCI AGREED THAT THE GOT HAD "CONSTRAINTS" ARISING FROM THE PRIME MINISTER'S PUBLIC COMMITMENT TO REGIONAL INCENTIVES AND RESISTANCE TO REDUCTION IN FREE TRADE ZONE TAX EXEMPTIONS, LED BY TRADE MINISTER TUZMEN. CANAKCI CONFIRMED IMF STAFF'S EARLIER COMMENTS THAT THE FUND TEAM WAS WORKING WITH GOT OFFICIALS TO DEVELOP A COMPROMISE. CANAKCI WAS OPTIMISTIC THAT LONG MEETINGS WEDNESDAY ON THIS ISSUE HAD BROUGHT THE TWO SIDES CLOSER TO AGREEMENT. CANAKCI SAID THERE WOULD BE A MEETING WITH THE PRIME MINISTER ON THE DIRECT TAX REFORM THURSDAY EVENING. ON FREE TRADE ZONES, THE COMPROMISE WOULD PHASE OUT EXEMPTIONS, PARTICULARLY ON PERSONAL INCOME TAX, THOUGH THERE WOULD BE SOME GRANDFATHERING OF ESTABLISHED COMPANIES.

LEGISLATION:

17. (SBU) THE PUBLIC SECTOR FINANCIAL MANAGEMENT AND CONTROL LEGISLATION HAS BEEN PREPARED. NOW THAT MINOR INTERAGENCY DISAGREEMENTS HAVE BEEN RESOLVED AND THE GOT HAS COME TO AN UNDERSTANDING WITH THE IMF TEAM, CANAKCI EXPECTED THE DRAFT LAW TO BE SUBMITTED TO PARLIAMENT ON MONDAY. THE AMENDMENT TO THE BANKRUPTCY LAW THAT WOULD ALLOW A CHAPTER 11-STYLE, PRE-PACKAGED BANKRUPTCY IS MOVING FORWARD, WITH IMF EXPERTS IN MEETINGS AT THE JUSTICE MINISTRY THURSDAY. CANAKCI EXPECTED THE LAW TO PASS BY END-NOVEMBER AND THE IMPLEMENTING REGULATIONS TO BE PROMULGATED IN DECEMBER.

18. (SBU) CANAKCI CONFIRMED THE IMF RESREP'S REPORT OF DELAYS IN PREPARATION OF THE LAW TO STRENGTHEN THE HAND OF BRSA IN GOING AFTER ASSETS OF OWNERS OF INTERVENED BANKS. AFTER BRSA PROPOSED A DRAFT TO DEPUTY PRIME MINISTER SENER'S OFFICE, SENER TURNED IT OVER TO MINISTER SAHIN, WHO IS RESPONSIBLE FOR GOVERNMENT-PARLIAMENT RELATIONS AND THE JUDICIARY. THE LAW SOMEHOW GOT BOGGED DOWN IN SAHIN'S OFFICE, SUCH THAT IT WILL NOT BE READY FOR SUBMISSION TO PARLIAMENT IN TIME FOR AN OCTOBER SIXTH REVIEW. NOW THAT THE PROCESS HAS BEEN REINVIGORATED WITH HELP FROM THE PRIME MINISTRY, CANAKCI SAID GOT ACTION ON THIS DRAFT LAW WOULD BE "RELEVANT" WERE THE SIXTH REVIEW TO COME TO THE IMF BOARD IN NOVEMBER RATHER THAN OCTOBER. COMMENT: POST WONDERS WHY THIS IMF REQUIREMENT WOULD NOT BE RELEVANT IF THE SIXTH REVIEW GOES TO THE IMF BOARD IN OCTOBER. END COMMENT. CANAKCI THOUGHT THERE MIGHT BE SOME NEED TO REVISE THE TEXT BECAUSE THE JUDICIAL AUTHORITIES OBJECTED TO TIME LIMITS IN THE LEGISLATION.

PRIVATIZATION:

19. (SBU) CANAKCI SAID PRIVATIZATION AUTHORITY PRESIDENT METIN KILCI BELIEVES THE TEKEL PRIVATIZATION WILL BE WRAPPED UP BY YEAR-END, POSSIBLY EVEN IN NOVEMBER. ON TURK TELECOM, CANAKCI SAID THE EVALUATION AND TENDERING COMMITTEES HAD DONE THEIR WORK BUT IT WAS NOT YET CLEAR WHEN THE PROPOSED STRATEGY WOULD GO TO THE COUNCIL OF MINISTERS.

IMAR BANK:

110. (SBU) THE TREASURY IS WAITING FOR THE SDIF (THE DEPOSIT GUARANTOR UNDER THE UMBRELLA OF BRSA) TO COMPLETE ITS FINDINGS ON THE COST OF PAYING IMAR BANK'S DEPOSITORS AND ON A FINANCING PLAN. CANAKCI SAID TREASURY, THE CENTRAL BANK AND BRSA ARE WORKING TOGETHER ON THIS AND HAVE LAID OUT THREE PRINCIPLES: 1) THE REPAYMENT PLAN SHOULD NOT PUT PRESSURE ON DOMESTIC INTEREST RATES AND PROJECTIONS FOR INTEREST PAYMENTS. 2) IT SHOULD NOT CREATE A DUTY LOSS ON STATE BANKS WHEN THE DEPOSITS ARE TRANSFERRED TO STATE BANKS. 3) IT SHOULD NOT PUT PRESSURE ON MONETARY TARGETS OR DETERIORATE THE BALANCE SHEET OF THE CENTRAL BANK. CANAKCI CONFIRMED THAT THE PLAN WILL MOST LIKELY INVOLVE TRANSFERRING THE DEPOSITS TO A STATE BANK, SUCH AS ZIRAAT BANK, AND THE TREASURY WOULD PROVIDE FUNDS TO EITHER PAY CASH TO DEPOSITORS OR PAY IN INSTALMENTS. EITHER WAY, THE PLAN WOULD RESULT IN AN INCREASE TO THE GOVERNMENT'S DEBT-TO-GDP RATIO. HE NOTED THAT THE CENTRAL BANK WOULD HAVE TO PROVIDE SOME LIQUIDITY FOR THE CASH PAYMENT PORTION.

WORLD BANK STRUCTURAL REFORMS:

111. (SBU) CANAKCI DID NOT DISPUTE ECONOFFS' SUGGESTION THAT THINGS SEEMED TO BE GOING BETTER WITH THE FUND THAN WITH THE BANK. CANAKCI ATTRIBUTED THE DIFFICULTIES TO THE NATURE OF THE BANK-SPONSORED STRUCTURAL REFORMS, WITHOUT ELABORATING. HE REFERENCED A BABACAN CONVERSATION WITH WOLFENSOHN AND WORLD BANK EUROPE DIRECTOR KATSU, SAYING THE GOT WOULD WORK ON SOME OF THE BANK ISSUES AFTER OCTOBER.

U.S. FINANCIAL AGREEMENT:

112. (SBU) CANAKCI REFERRED TO THE TREASURY-TO-TREASURY UNDERSTANDING IN DUBAI THAT THE GOT MIGHT REQUEST A DISBURSEMENT IN THE SECOND WEEK OF OCTOBER. HE CONFIRMED, HOWEVER, THAT TREASURY HAD NOT YET SUBMITTED THE AGREEMENT TO THE COUNCIL OF MINISTERS FOR RATIFICATION, AND COULD NOT SAY WHEN IT WOULD DO SO. WHEREAS CANAKCI'S SUBORDINATE OZGUR PEHLIVAN HAD EARLIER TOLD ECONOFF THAT THERE WAS NO NEED FOR PARLIAMENTARY APPROVAL OF THE FA UNDER TURKISH LAW, CANAKCI'S ONLY COMMENT WAS, "SOME PEOPLE ARE NOW SAYING THE FA NEEDS PARLIAMENTARY APPROVAL." HE ALSO NOTED THAT THE TREASURY WAS IN A COMFORTABLE CASH-FLOW POSITION FOR THE REMAINDER OF THE YEAR.

113. (SBU) CANAKCI ALSO REFERRED TO THE TREASURY'S CONCERNS ABOUT THE INTEREST RATE, CHUCKLING OVER THE OMB CALCULATION METHODOLOGY BEING A "BLACK BOX." THOUGH CANAKCI ADMITTED THE RATE WAS LOWER THAN WHAT THE GOT COULD GET IN THE MARKET, HE NOTED THAT TURKEY'S BORROWING RATES WERE TRENDING DOWNWARDS, SUCH THAT THEY MIGHT REACH THE LEVEL IN THE FA.

114. (SBU) ECONOFFS REMINDED CANAKCI OF THE DETAILED INFORMATION REQUIREMENTS IN SCHEDULE C OF THE AGREEMENT THAT THE USG WOULD NEED TO RECEIVE WHEN THE GOT REQUESTED A DISBURSEMENT. ECONOFFS SUGGESTED MUCH OF THE SAME INFORMATION THAT WAS UNDOUBTEDLY BEING DEVELOPED FOR THE IMF MISSION COULD BE PROVIDED TO THE USG. ECONOFFS STRESSED THAT THE USG WANTED TO HELP TURKEY, BUT THAT IT WAS CRITICAL FOR THE GOT TO BE ABLE TO MAKE A CONVINCING CASE THAT THE REFORMS WERE MOVING FORWARD. CANAKCI REPLIED THAT BEING ON TRACK WITH THE IMF WAS THE MOST VISIBLE INDICATOR THAT THE GOT WAS IMPLEMENTING STRONG ECONOMIC POLICIES.

INVESTMENT:

115. (SBU) ECONOFFS NOTED GOT LEGAL REFORMS TO IMPROVE THE INVESTMENT CLIMATE BUT ALSO POINTED OUT THE ABSENCE OF RESOLUTION OF SPECIFIC U.S. COMPANIES' PROBLEMS. CANAKCI SAID THE HIGH INVESTORS' COUNCIL (YOIK) WAS A VEHICLE TO HEAR FOREIGN INVESTORS' COMPLAINTS. HE SAID THAT FOREIGN COMPANIES

HAD MADE PRESENTATIONS TO YOIK AND ENCOURAGED U.S. COMPANIES
TO DO SO. CANAKCI CLAIMED THAT TREASURY WAS DOING ITS BEST ON
THE INVESTMENT CLIMATE.

EDELMAN